IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 420

GIBRALTOR AMUSEMENTS, LTD., *Petitioner*,

v.

THE WURLITZER COMPANY AND WURLITZER ACCEPTANCE CORPORATION, *Respondents*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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September 21, 1961.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above-entitled proceeding on May 24, 1961.

CITATION TO OPINIONS BELOW

The opinion of the Court of Appeals rendered on May 24, 1961, is reported at 291 F. 2d 22 and is reprinted as Appendix A hereto. The opinion of the District Court for the Eastern District of New York

(Bartels, J.) is reported at 187 F. Supp. 931 and is reprinted as Appendix B hereto.

JURISDICTION

The judgment of the Court of Appeals was entered on May 24, 1961. On August 16, 1961, Mr. Justice Frankfurter signed an order extending the time for filing this petition for writ of certiorari to and including September 21, 1961. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTION PRESENTED

Whether, under Section 59(b) of the Bankruptcy Act, a petitioning creditor's wholly owned subsidiary, to which the parent creditor has assigned certain claims against the debtor prior to the filing of the bankruptcy petition, can be counted as one of the three petitioning creditors essential to the maintenance of an involuntary petition in bankruptcy.

STATUTE INVOLVED

Section 59(b) of the Bankruptcy Act, 11 U.S.C.A. § 95(b), entitled "Who may file and dismiss petitions", reads as follows:

"Three or more creditors who have provable claims liquidated as to amount and not contingent as to liability against any person which amount in the aggregate in excess of the value of securities held by them, if any, to $500 or over, or, if all of the creditors of such person are less than twelve in number, then one or more of such creditors whose claim or claims equal such amount, may file a petition to have him adjudged a bankrupt."

STATEMENT OF THE CASE

The petitioner, Gibraltor Amusements, Ltd., is the alleged bankrupt in this proceeding.

On March 18, 1960, an involuntary petition in bankruptcy was filed by the respondent Wurlitzer Company as a sole creditor, alleging less than twelve creditors of the bankrupt.[1] The bankrupt filed an answer on March 29, 1960, denying *inter alia* that there were less than twelve creditors. An amended involuntary petition was then filed by the Wurlitzer Company on May 5, 1960, again alleging less than twelve creditors. Thereupon one William F. Wadsworth and the Wurlitzer Acceptance Corporation (WAC) were granted leave to intervene and join as petitioning creditors. The amended answer, filed on May 10, 1960, reiterated the denial of the allegation as to twelve creditors and asserted (R. 19a) that "Wurlitzer Acceptance Corporation, an intervening creditor, is a wholly owned subsidiary of the petitioning creditor and as such does not qualify as an independent, separate petitioning creditor."

The matter was then referred to a Referee in Bankruptcy. The trial before the Referee was narrowed by concessions to the sole issue "of whether a sufficient number of qualified creditors have joined in the petition for involuntary bankruptcy, at least three qualified creditors being required as the record disclosed that the alleged bankrupt had twelve creditors or more on March 18, 1960." R. 21a.

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[1] R. 2a. The record references herein are to Volume 1 of the certified record, consisting of the appendix to petitioner's brief in the Court of Appeals.

The Referee, upon the conclusion of the trial, made the following pertinent findings and conclusions:

(1) WAC, the intervening creditor, is a Delaware corporation and a wholly owned subsidiary of Wurlitzer. R. 23a. "It was organized in 1957 for the primary purpose of financing sales of Wurlitzer products. It finances all sales generated by the retail music stores owned and operated by the parent company, as well as sales made by Wurlitzer dealers, distributors and operators. It is a distinct legal entity separate and apart from its parent corporation. It acquired the notes and security long prior to the bankruptcy." R. 23a.

(2) More than $1,000,000 was owed by the bankrupt to Wurlitzer, the indebtedness being in the form of defaulted promissory notes secured by conditional sales contracts. Wurlitzer had acquired these notes and contracts as a holder in due course and they constituted valid and subsisting liens against the bankrupt and its property. R. 22a.

(3) Two of the aforesaid promissory notes had been acquired by WAC in the regular course of its business by assignment from Wurlitzer. One note had been so acquired on October 31, 1958, and the other on May 28, 1958; on the date of filing the bankruptcy petition (March 18, 1960) these notes were in default in the respective amounts of $5,261 and $4,785. R. 24a. On May 15, 1959, the bankrupt had executed and delivered a written guaranty of payment to Wurlitzer of certain obligations, including the notes in question. The Referee concluded that this guaranty "expressly extended not only to Wurlitzer but to its 'successors and assigns' and thus included WAC" and that upon the assignment of the two notes to WAC the latter "became entitled to the benefit of the alleged bankrupt's guaranty." R. 24a-25a.

(4) Finding that the assignment by Wurlitzer to WAC of the two notes without recourse "was sufficient to transfer title to WAC" and give the latter a right of action against the bankrupt, the Referee concluded that "WAC is a creditor of the alleged bankrupt, and in every respect qualified to act as a petitioning creditor herein." R. 25a.

The Referee, having found that Wurlitzer, WAC and two individuals qualified as petitioning creditors and that the total number of creditors was more than twelve, held that the petitioning creditors were entitled to an order adjudging the petitioner herein to be a bankrupt. R. 28a. An order to that effect was duly entered. R. 29a-30a.

Upon a petition for review filed by the bankrupt, the District Court affirmed the order adjudging petitioner a bankrupt, except that it overruled the Referee's finding and conclusion that one of the individuals qualified as a petitioning creditor. R. 34a-43a. As a result, the bankruptcy adjudication was sustained on a finding that there were three qualified petitioning creditors—the minimum number required to sustain an involuntary petition in these circumstances. As to the petitioner's objections to counting WAC as one of those three, the District Court ruled that WAC was qualified as a separate entity, there being no proof that the parent Wurlitzer Company had employed WAC for an illegal purpose or as a front so as to justify piercing WAC's corporate veil. R. 39a-40a.

The Court of Appeals affirmed by a two-to-one vote, Judge Friendly dissenting. The majority held that WAC should be counted as an independent petitioning creditor in the absence of any showing that Wurlitzer had in some way used WAC to subvert the Bank-

ruptcy Act. Judge Friendly wrote that it was contrary to the history and purpose of the Act to regard a parent and a subsidiary as separate entities in counting the requisite number of petitioning creditors in involuntary proceedings, even in the absence of any proof of fraud or intent to subvert the Act.

REASONS FOR GRANTING THE WRIT

The decision below raises an important, unresolved and recurring problem in the administration of the Bankruptcy Act that needs definitive resolution by this Court.

Under Section 59(b) of the Bankruptcy Act, 11 U.S.C.A. § 95(b), where there are more than twelve creditors of the debtor, "it is indispensable to the maintenance of the [involuntary] petition that the existence of three petitioners holding provable claims be established, if challenged." *Canute Steamship Co.* v. *Pittsburgh & West Virginia Coal Co.*, 263 U.S. 244, 248. And see *Meek* v. *Centre County Banking Co.*, 268 U.S. 426, 431, note 3. The problem here is whether a wholly owned subsidiary of a petitioning creditor can be counted as one of the three necessary petitioners on the basis of its purchase of certain claims against the debtor from its parent corporation.

The majority of the Court sought to answer that question affirmatively by relying upon the proof in this case that WAC, the wholly owned subsidiary, is an entity separate and distinct from its parent Wurlitzer Company and upon the complete absence of any indication that Wurlitzer had abused or disregarded WAC's independence. In the absence of some showing of a fraudulent subversion of the "rule of three" provision of the Bankruptcy Act, said the court, WAC's status as a petitioning creditor must be honored.

But the basic question remains whether, if it be assumed that WAC was independent of Wurlitzer and acquired the claims from Wurlitzer in the normal course of its legitimate business, such related enterprises can be counted as two separate petitioning creditors for purposes of Section 59(b) of the Bankruptcy Act. And the answer to that critical problem is not to be found in the general provisions of contract or tort law giving recognition to the independent status of such parents and subsidiaries. See *Owl Fumigating Corp.* v. *California Cyanide Co.*, 30 F. 2d 812, 813 (C.A. 3). Nor is it to be found in decisions refusing to pierce the corporate distinctions of such related organizations in other statutory contexts. And by the same token, disregarding the corporate distinctions in any setting other than Section 59(b) of the Bankruptcy Act brings no solution to this problem. As stated in *Scheuley Distillers Corp.* v. *United States*, 326 U.S. 432, 437: "While corporate entities may be disregarded where they are made the implement for avoiding a clear legislative purpose, they will not be disregarded where those in control have deliberately adopted the corporate form in order to secure its advantages and *where no violence to the legislative purpose is done by treating the corporate entity as a separate legal person.*" [Emphasis added.][2]

The essence of the problem thus is whether treating a wholly owned independent subsidiary, that has purchased a debt from its parent, as a creditor separate from its parent creditor corporation does violence to

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[2] Some of the relevant considerations in determining whether separate entities constitute one economic enterprise are listed in *Labor Board* v. *Deena Artware, Inc.*, 361 U.S. 398, 402-404. See also *Chicago, M. & St. P. R. Co.* v. *Minneapolis Assoc.*, 247 U.S. 490, 501.

the legislative purpose expressed in Section 59(b) of the Bankruptcy Act. The majority below merely said that if Congress meant Section 59(b) to alter the ordinary judicial rules recognizing the separate status of wholly owned subsidiaries "it should have so provided specifically." But the presence or absence of specific words may not be the solution to this type of statutory problem, particularly since the legislative words here permit conflicting interpretations. See *Burnet* v. *Guggenheim*, 288 U.S. 280, 285.

The answer may well lie in Judge Friendly's analysis of the Congressional background of Section 59(b), an analysis showing that this provision represented a compromise "between those who wanted to give the creditor an effective remedy to assure equal distribution of a bankrupt's assets and those who were determined to protect the debtor from the harassment of ill-considered or oppressive involuntary petitions, including those by a single creditor interest." On the basis of his examination of the legislative record, Judge Friendly concluded that the thrust of Section 59(b), as a compromise of opposing forces, was "to require three separate creditor interests, separate in reality and not merely in form."

The issue is thus squarely joined in this case. On the record there has been found no indication that WAC was other than an independently operated subsidiary or that it acquired its claims other than in the normal course of its legitimate business. But neither is there any question as to its being wholly owned by Wurlitzer or as to its having acquired its creditor status solely by purchase of debt claims from Wurlitzer. These may be separate legal entities but there is in fact but one creditor interest. And the problem

is inescapably raised in its purest form—whether Congress meant to require three creditor entities or three separate creditor interests.

If the majority's view be adopted, anomolous results could follow. As Judge Friendly pointed out, a single creditor corporation, for good business reasons, could parcel out some of its debt claims to two or more financing subsidiaries and thus insure its ability to initiate an involuntary bankruptcy proceeding should there be more than twelve creditors. By so doing, the creditor corporation would in effect be creating three creditors where originally there was only one. A single creditor interest could thus become dominant even in the absence of any intent to subvert the "rule of three." And the statutory policy of protecting the possible desire of the twelve or more other creditor interests (especially those having no preferences) to have the business continue free of bankruptcy proceedings becomes subordinated to the wishes of this single creditor interest. The "rule of three" could accordingly become meaningless.

The concentration of power thus placed in the hands of a parent corporation that disposes of some of its debt claims to its subsidiaries—or even to unaffiliated corporations—raises an increasingly important problem in the administration of the Bankruptcy Act. As the creation and use of wholly owned financing subsidiaries become more prevalent in the United States, precisely the kind of problem posed by this case will become more frequent in bankruptcy proceedings. The court below, perhaps the most experienced tribunal in the country in bankruptcy matters, has been unable to provide a clear-cut solution. So significant a problem thus deserves the plenary consideration that only this Court can give to it.

Certainly this issue is no less significant for certiorari purposes than the question which led to the grant of certiorari in *Canute Steamship Co.* v. *Pittsburgh & West Virginia Coal Co.*, 263 U.S. 244, the question there being whether subsequent intervening creditors could be counted in determining whether, under Section 59 (b), there was compliance with the "rule of three."

CONCLUSION

For the foregoing reasons this petition for a writ of certiorari to review the judgment of the Court of Appeals for the Second Circuit should be granted.

Respectfully submitted,

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APPENDIX A

In the Matter of GIBRALTOR AMUSEMENTS, LTD., Bankrupt-Appellant,

and

The Wurlitzer Company and Wurlitzer Acceptance Corporation, Petitioning Creditors, Appellees.

No. 319, Docket 26812.

United States Court of Appeals
Second Circuit.

Argued March 22, 1961.
Decided May 24, 1961.

George Becker, New York City, for bankrupt-appellant.

Edward R. Neaher, New York City (Chadbourne, Parke, Whiteside & Wolff, New York City and Charles J. Prentiss, New York City, on the brief), for Wurlitzer Co. and Wurlitzer Acceptance Corp., appellees.

Before MOORE, FRIENDLY and SMITH, Circuit Judges.

J. JOSEPH SMITH, Circuit Judge.

Gibraltor Amusements, Ltd., the alleged bankrupt, is the operator of numerous "Juke Box" routes on Long Island. The Wurlitzer Company, principal creditor of the alleged bankrupt for a sum exceeding $1,000,000, filed an involuntary petition in bankruptcy against Gibraltor in March of 1960. The petition alleged insolvency, numerous acts of bankruptcy and that the debtor had fewer than twelve creditors. Gibraltor's answer denied the claimed indebtedness, challenged Wurlitzer's standing on the ground that it had been the recipient of preferential payments and denied there were fewer than a dozen creditors. Bankruptcy Act, § 59, subs. b, d, 11 U.S.C.A. § 95, subs. b, d. In support of its last cited contention, Gibraltor submitted a list of its creditors on the date of the petition. To counter this, Wur-

litzer subsequently moved to amend its petition—which motion was granted. The bankruptcy court also granted leave to Wurlitzer Acceptance Corporation (WAC), William F. Wadsworth and Joseph Rae to file as intervening creditors.

After a hearing, Referee Castellano decided all of the issues against the bankrupt. He held that the alleged debts and acts of bankruptcy had been amply proven, that Wurlitzer's petition was not a sham or a fraud on the court and that Wurlitzer, although secured for the larger portion of its claims, was an unsecured creditor for a sum far in excess of $500. Without deciding that certain installment payments made to Wurlitzer were preferential, the referee ruled that a preferred creditor has a "provable" claim so as to satisfy the requirements of §59 sub. b, even though the claim is not "allowable" unless the preference is surrendered. Winkleman v. Ogami, 9 Cir., 1941, 123 F.2d 78. Cf. In re Automatic Typewriter & Service Co., 2 Cir., 1921, 271 F. 1. Finally, Referee Castellano found that Rae, Wadsworth and WAC all qualified as petitioning creditors and duly adjudged Gibraltor a bankrupt. On a Petition for Review to the District Court for the Eastern District of New York, Judge Bartels upheld the referee's findings in all particulars save the Rae petition. As to that, the court held that Rae's claim was "contingent as to liability," [187 F.Supp. 937] thereby disqualifying him as a petitioner. Because three petitioning creditors still remained, however, the court confirmed the adjudication of bankruptcy.

On appeal to this court, appellant has renewed all of his contentions below. There is absolutely no merit in most of them. The referee's various factual findings as to Gibraltor's insolvency, Wurlitzer's partially unsecured status and the existence of the Wadsworth debt are amply supported by the record; they surely are not "clearly erroneous" as they must be to warrant reversal. Margolis v. Nazareth Fair Grounds & Farmers Market, Inc., 2 Cir., 1957, 249 F.2d 221; Stim v. Simon, 2 Cir., 1960, 284 F.2d 58; In re Tabibian, 2 Cir., 289 F.2d 793. The only substantial question raised is the standing of WAC as a separate petitioning creditor.

Wurlitzer Acceptance Corporation is a wholly owned subsidiary of the Wurlitzer Company. It was incorporated in 1957 and its business has been the financing of sales of the parent's products. Although WAC appears to have dealt solely in the commercial paper of Wurlitzer, it has obtained its own bank financing—on the strength of its own credit. It has been a separate corporate taxpayer for the purposes of the Federal income tax. The evidence indicates that both parent and subsidiary have scrupulously honored the separate corporate form of the latter. WAC's claim is for almost $17,000 on two notes guaranteed by Gibraltor. The notes had been purchased from Wurlitzer long before the filing of the petition; there is absolutely no evidence of attempted subversion of the Bankruptcy Act.

For most purposes, the law deals with a corporation as an entity distinct from its shareholders. Traditionally courts will pierce the corporate veil "when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime." United States v. Milwaukee Refrigerator Transit Co., C.C.E.D.Wis.1905, 142 F. 247, 255; In re Belt-Modes, Inc., D.C. S.D.N.Y.1950, 88 F.Sup. 141; Rapid Transit Subway Construction Co. v. City of New York, 1932, 259 N.Y. 472, 182 N.E. 145. Although courts will sometimes disregard the separate entity where it has been used as a "front" or a "mere conduit"—the so-called alter ego doctrine—the present case with its complete absence of fraud and strict honoring of the corporate form as to assets and intercorporate transactions[1] is not a proper one for the invocation of that rule. See In re Belt-Modes, Inc., supra, 88 F.Supp. at page 144; Shamrock Oil & Gas Co. v. Ethridge, D.C.D.Colo.1958, 159 F.Supp. 693, 697; Western Electric Co. v. Cinema Supplies, 8 Cir., 1935,

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[1] Apparently Wurlitzer handled most of WAC's collections for it while it collected on its own notes. Such an arrangement was undoubtedly cheaper and more efficient and is not enough from which to infer an internal disregard of WAC's separate entity.

80 F.2d 106, 108; 1 Fletcher Cyc. Corp., Perm.Ed. §§ 41, 43.[2]

Since ordinary principles of the law of corporations do not warrant the disregard of WAC's corporate identity here, it remains only to ascertain whether anything in the language or policy of the Bankruptcy Act demands such a result. Section 59, sub. b, 11 U.S.C.A. § 95, sub. b provides simply that "Three or more *creditors* who have provable claims liquidated as to amount and not contingent as to liability against any person * * * may file a petition to have him adjudged a bankrupt." "Creditor" is defined in § 1(11), 11 U.S.C.A. § 1(11) as follows: " 'Creditor' shall include *anyone who owns a debt, demand, or claim* provable in bankruptcy * * * "

The aforecited language, far from being restrictive in its definition of the scope of permissible petitioners, is virtually all encompassing. The emergence of the wholly owned corporate subsidiary as a common business instrumentality is not a brand new phenomenon. While Congress has repeatedly added to and amended the Federal taxing laws to deal with problems posed by the multiple corporation means of doing business, it has not seen fit similarly to tinker with the Bankruptcy Act. The detailed ground rules for "counting creditors" laid down by § 59, sub. e, 11 U.S.C.A. § 95, sub. e indicate that the principal Congressional fear of abuse was not that a debtor would be too easily petitioned into bankruptcy—rather than through connivance with friendly creditors the insolvent debtor might be able unfairly to hamstring one or two large creditors. The courts have long evinced a disposition to honor the separate corporate entity in bankruptcy matters; Comstock v. Group of International Investors, 1948, 335 U.S. 211, 68 S.Ct. 1454, 92 L.Ed. 1911; In re Belt-Modes, Inc., supra. If Congress meant to alter ordinary judicial rules governing corporations, it should have so provided specifically.

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[2] "One corporation may be disregarded where the two are identical or indistinguishable in fact. Unless it is a mere instrumentality or agency or adjunct in that sense, or as a sham or is used in fraud, by the dominant corporation, it will not be disregarded; and it will not be disregarded unjustly." 1 Fletcher Cyc. Corp. 155.

Whether the policy of the Act calls for a more narrow construction of qualified "creditors" is a closer question. The present requirement of three petitioning creditors, inserted in the Act of 1898, is a compromise between the quite liberal provision of the Act of 1841 and the restrictive requirements of the 1867 Act. 3 Collier on Bankruptcy 548. In the process of "counting to three," the courts have perhaps been overly liberal in allowing the holders of assigned claims to qualify as practitioners. See In re Bevins, 2 Cir., 1908, 165 F. 434, where the court allowed the petitions of two assignees who had taken claims for the specific purpose of making up the required statutory number. General Order 5(2), 11 U.S.C.A. following section 53, while recognizing assignees as petitioners, set up a check against abuse of the assignment device by requiring an affidavit setting forth the particulars of the transfer.[3]

It may be conceded to be highly questionable whether Congress meant to sanction traffic in claims merely for the purpose of creating a sufficient number of petitioning creditors. While such was the case in Bevins, and was there approved, no such machinations have been presented in the instant case. Even though WAC took the notes in the due course of business, without reference to any future bankruptcy proceeding, it is urged that the mere fact of "control" by Wurlitzer disqualifies the subsidiary's claim. This argument merely raises, in a slightly different guise, the question of the disregard of the subsidiary's separate entity. There has been no showing, however, that Wurlitzer has abused the distinct corporate form nor that it has used it fraudulently to subvert the Bankruptcy Act. Lacking such a showing, WAC's claim should be honored. Such an ap-

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[3] General Order 5(2) provides: "Petitioners in involuntary proceedings for adjudication, whose claims rest upon assignment or transfer from other persons, shall annex to one of the triplicate petitions all instruments of assignment or transfer, and an affidavit setting forth the true consideration paid for the assignment or transfer of such claims and stating that the petitions are the bonafide holders and legal and beneficial owners thereof and whether or not they were purchased for the purpose of instituting bankruptcy proceedings."

proach to this question is not a purely conceptual one; it must be kept in mind that protection of the separate creditors of WAC, who cannot reach the assets of Wurlitzer, can only be accomplished by the recognition of the subsidiary as an independent legal entity.

Affirmed.

FRIENDLY, Circuit Judge (dissenting).

With some regret as regards this particular bankrupt, I respectfully dissent from the conclusion that Wurlitzer and its wholly owned subsidiary, Wurlitzer Acceptance Corporation (WAC), may be regarded as two separate creditors for the purpose of § 59, sub. b of the Bankruptcy Act, 11 U.S.C.A. § 95, sub. b.

Assuming as I do that WAC had sufficient independence of its parent to be regarded as a separate corporation under state law in contract or tort litigation, Bartle v. Home Owners Co-Op, Inc., 1955, 309 N.Y. 103, 127 N.E.2d 832, or under federal law for income tax purposes, it does not follow that it is a creditor separate from its parent under § 59, sub. b. It is too often forgotten that whether a subsidiary corporation is to be deemed a separate entity "cannot be asked, or answered, *in vacuo*," Latty, The Corporate Entity as a Solvent of Legal Problems, 34 Mich.L.Rev. 597, 603 (1936); the issue in each case must be resolved by reference to the policy of the applicable statutory or common law rule. See, e. g., Hart Steel Co. v. Railroad Supply Co., 1917, 244 U.S. 294, 37 S.Ct. 506, 61 L.Ed. 1148; Chicago, etc., Ry. Co. v. Minneapolis Civic & Commerce Ass'n, 1918, 247 U.S. 490, 38 S.Ct. 553, 62 L.Ed. 1229. Although my brothers recognize that the requirement of three petitioning creditors in the Bankruptcy Act of 1898 (save where the bankrupt had less than twelve creditors) was a compromise by Congress between the divergent provisions of earlier statutes, that bland statement scarcely conveys the flavor. "In law also the emphasis makes the song." Bethlehem Steel Co. v. New

York State Labor Relations Board, 1947, 330 U.S. 767, 780, 67 S.Ct. 1026, 1033, 91 L.Ed. 1234.

The first three bankruptcy acts, all repealed after relatively short periods, permitted a single creditor to initiate involuntary proceedings if his claim met the prescribed minimum.[1] Widespread sentiment against the 1867 Act, which not only allowed a single creditor to institute involuntary proceedings but provided for numerous acts of bankruptcy and, in the absence of creditor consent, denied a discharge from debts to a bankrupt who could not pay fifty cents on the dollar, MacLachlan, Bankruptcy (1956), p. 11, caused Congress to amend it in 1874, 18 Stat. 178, 181. In addition to making discharges less difficult to obtain and narrowing the acts of bankruptcy, the amendment provided that an involuntary petition could be filed only by one fourth of the total number of creditors with aggregate claims amounting to one third of the dollar amount of the total debts. Still the statute was too harsh for debtor sentiment, and it was repealed in 1878, see 3 Collier on Bankruptcy, p. 548.

The impulse for a new bankruptcy law came from the 200,000 business failures in the United States between the 1878 repeal of the 1867 Bankruptcy Act and 1898. Hardship had been particularly acute in the West, where a great land boom had raged from 1883 to 1889, followed by a sharp collapse. Southern and Western Populists began a crusade for at least a temporary voluntary bankruptcy law to relieve the large numbers of honest debtors from oppressive burdens and give them a fresh start in life. See Representative Sparkman of Florida, 31 Cong.Rec. 1850.

Although Eastern congressmen were willing to concede that voluntary bankruptcy was a good idea see Representative Parker (N.J.), 31 Cong.Rec. 1852, many of them were unwilling to enact a voluntary bill without accompanying involuntary features designed to insure an equitable distri-

[1] In the Act of 1800, 2 Stat. 19, the amount was $1,000; in the 1841 act, 5 Stat. 440, it was $500; in the 1867 act, 14 Stat. 517, 536, $250.

bution of a bankrupt's assets among his creditors, and, to that end, to abolish preferences. This the Populists opposed. They argued there was no need to infringe on state rights by creating a federal remedy for the collection of debts: state laws were adequate for the purpose. Bankruptcy was viewed as a stigma difficult to erase; it was one thing to allow a hopelessly burdened debtor to choose this disagreeable alternative as preferable to eternal debt but quite another to permit blood-thirsty creditors, with only their own interests at heart, to plunge an unwilling debtor into disgrace—the more so since in many cases the debtor reasonably might hope that the upturn in his fortunes was just around the corner, and bankruptcy would deprive him of the right to keep his business alive in the meantime. See 31 Cong.Rec. 1793 (Underwood, Ala.), 1838 (Settle, Ky.), 1863 (Linney, N. C.), 2313 (Sen. Stewart, Nev.). This position was summed up by Representative Lewis of Georgia, 31 Cong.Rec. 1908: "Voluntary bankruptcy is the means of redemption of the unsuccessful and fallen debtor. Involuntary bankruptcy is a weapon in the hands of the creditor to press collections of debt harshly, to intimidate, and to destroy."[2] Thus the Populists denounced the bankruptcy bill as an "engine of oppression" (Sparkman, Fla., 31 Cong. Rec. 1851), "intended to bind hand and foot the debtors of this country and place them in the vise-like grip of the greedy cormorants of the country" (Henry, Tex., 31 Cong. Rec. 1803), and even tied the issue to the silver question, haranguing the "conspiracy of gold and monopoly" (Sen. Stewart, Nev., 31 Cong.Rec. 2359–60).[3] Easterners coun-

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[2] Seventy years earlier, in 1827, Martin Van Buren, denouncing an attempt to provide for voluntary and involuntary bankruptcy in a single statute, had said "It is an erroneous idea * * * that this bill can be made to serve God and mammon by combining two things totally at variance." 3 Cong.Deb. 279.

[3] Some idea of the intensity of the feeling is conveyed by the remarks of Senator Stewart of Nevada against "this diabolical bill," 31 Cong.Rec. 2312; "This bill comes from the class of men who are grinding the face of the poor * * * (2362). This is a bill which belongs to the Dark Ages. It belongs to the age of the Inquisition; it belongs to the age of witchcraft * * *. It is dictated by the same spirit that hung and killed and drew and quartered women for witchery" (2408).

tered that a properly restricted involuntary bankruptcy law was a benefit not only to creditors but to debtors as well. In the absence of such a law creditors become nervous; whenever the debtor's assets seem less than his liabilities, they are likely to grab them precipitously, thereby forcing the debtor to the wall, lest other creditors beat them to the draw and they get nothing. 31 Cong.Rec. 1789 (Henderson, Iowa), 1852 (Parker, N. J.).

The provisions of the statute with respect to involuntary bankruptcy were the resulting vector of these opposing forces, an attempt to make involuntary bankruptcy less unpalatable to the Populists by surrounding such proceedings with careful safeguards for the debtor. The original bill in the 55th Congress, S. 1035, provided for three petitioning creditors if the total were twelve, just as in the present law. But in other respects the bill was too harsh toward debtors to suit the Senate. Although the substituted bill passed by that body, which reduced the number of criminal offenses, the acts of bankruptcy, and the causes for denying a discharge, permitted an involuntary petition to be filed by "a creditor or creditors having debts against such a bankrupt to the amount of $500 or more," as in the acts prior to 1874, the House Judiciary Committee substituted a bill more like that originally introduced in the Senate. This bill was bitterly debated in the House for more than 100 pages in the Record. Its proponents attempted to sugar-coat the pill by repeated reference to a number of safeguards inserted to protect debtors from oppressive use of the weapon of involuntary bankruptcy: to be insolvent one must have assets insufficient to pay his debts, not merely insufficient liquid funds to meet debts as they fall due; oppressive costs of proceedings under the 1867 act had been drastically pruned; petitioning creditors were required to post bonds to cover not only the costs of the proceedings but any damages that might result from a wrongful filing; widows, minors and the insane were protected; the bankrupt could be taken into custody only if he showed signs of departing to avoid examination; he might not be required to travel over 100

miles to testify; criminal offenses and acts of bankruptcy were reduced; and three creditors must join if there were twelve or more in all. H.R.Rep. No. 65, 55th Cong., 2d Sess., 25–27 (1897). An attempt was made by Representative Livingston of Georgia to require "that no man can be placed in bankruptcy except on a petition signed by two-thirds of his creditors representing two-thirds of the indebtedness," 31 Cong.Rec. 1791. But Representative Henderson, chairman of the Judiciary Committee, which reported the substitute bill, responded that the present bill "goes far enough, if not too far, in restraining creditors from moving, having to give bonds with sureties." Ibid. The House passed this version; a conference committee toned it down in several respects to make it more favorable to the debtor; and both houses enacted the conference bill.

Thus, the entire process that resulted in the enactment of the Act of 1898 was a pitched battle between those who wanted to give the creditor an effective remedy to assure equal distribution of a bankrupt's assets and those who were determined to protect the debtor from the harassment of ill-considered or oppressive involuntary petitions, including those by a single creditor interest. The requirement of three creditors was one of many provisions reflecting a compromise between the two opposing positions. It is not doing justice to this history to suggest that if Congress had meant to prevent a wholly owned subsidiary from being counted as a petitioning creditor separate from its parent, it should have explicitly said so.[4] We must "remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning." Cabell v. Markham, 2 Cir., 1945, 148 F.2d 737, 739, affirmed 1945, 326 U.S. 404, 66 S.Ct. 193, 190

[4] It should also be remembered that at common law a corporation could not hold stock in other corporations unless the power was expressly conferred; the extensive development of the use of subsidiaries apparently began with the New Jersey Act of 1888, pp. 385, 445, conferring the power in general terms. See 1 Hornstein, Corporate Law and Practice, § 111.

L.Ed. 165. Here the purpose to require three separate creditor interests, separate in reality and not merely in legal form, is not difficult to discern. With the temper of the 55th Congress on this subject, it would have required a bold man to arise on the floor of the House of Representatives and ask that the bill be clarified to insure that a corporation with a financing subsidiary could be counted as two creditors if each unit held a claim against the debtor; it is hard to suppose the House managers would have imperiled the bill by sanctioning any such proposal and quite impossible to believe it would have been enacted. Yet, where the words permit either interpretation, our duty is to determine "which choice is it the more likely that Congress would have made." Burnet v. Guggenheim, 1933, 288 U.S. 280, 285, 53 S.Ct. 369, 370, 77 L.Ed. 748.

Comstock v. Group of International Investors, 1948, 335 U.S. 211, 68 S.Ct. 1454, 92 L.Ed. 1911, especially when read in the light of Taylor v. Standard Gas & Electric Co., 1939, 306 U.S. 307, 59 S.Ct. 543, 83 L.Ed. 669, does not support any view that a court of bankruptcy will regard parent and subsidiary as different entities *semper et ubique*; rather it held that on the facts the particular policy there applicable did not require that they be regarded as the same, as in the Taylor case to some extent the same policy had. Here we deal with a different policy—that only three distinct creditors may precipitate an involuntary bankruptcy of a debtor having more than twelve.[5] I cannot believe it consistent with that policy to hold that a single creditor corporation may insure its ability to initiate an involuntary bankruptcy by the simple expedient of organizing two financing subsidiaries—perhaps with independent creditors—and seeing to it that claims against each debtor are parceled out in ad-

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[5] If my brothers' reference to In re Bevins, 2 Cir., 1908, 165 F. 434 indicates a view that the decision in that case ought be reexamined, I wholeheartedly agree. However, it can stand without requiring an affirmance here.

vance of bankruptcy.[6] See In re Supreme Tool & Mfg. Co., D.C.E.D.Wis. 1956, 147 F.Supp. 158. Whether a wholly owned subsidiary with independent creditors might be deemed separate from its parent in a case where, as a result of its own financial difficulties, the subsidiary was in effect acting for its creditors rather than its stockholders, need not be now determined; no such case is presented here.

UNITED STATES COURT OF APPEALS

For The

Second Circuit

As a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-fourth day of May, one thousand nine hundred and sixty-one.

Present:

HON. LEONARD P. MOORE
HON. HENRY J. FRIENDLY
HON. J. JOSEPH SMITH
Circuit Judges

In
the Matter of

GIBRALTOR AMUSEMENTS, LTD.,
Bankrupt-Appellant.

Appeal from the United States District Court for the Eastern District of New York.

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[6] It could be said in such a case also that there was no evidence of abuse of the corporate form with a purpose fraudulently to subvert the Bankruptcy Act; bankruptcy of the debtor might have been the furthest thing from contemplation when the claims were placed and there may have been good business reasons for doing so.

This cause came on to be heard on the transcript of record from the United States District Court for the Eastern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed; with costs to the appellees.

A. DANIEL FUSARO,
Clerk

APPENDIX B

Opinion of Bartels, D. J. on Review Sustaining the Referee.

[SAME TITLE.]

Appearances:

CHADBOURN, PARKE, WHITESIDE & WOLFF, Esqs., Attorneys for The Wurlitzer Company and Wurlitzer Acceptance Corporation, Petitioning Creditors
EDWARD R. NEAHER, Esq. of Counsel.
GEORGE BECKER, Esq., Attorney for Bankrupt.

BARTELS, D. J.

This is a petition by Gibraltor Amusements, Ltd. for review under Section 39(c) of the Bankruptcy Act, 11 U.S.C.A. Sec. 67(c), of the Referee's Order of August 19, 1960, adjudicating Gibraltor a bankrupt. The Order was based upon the Referee's well reasoned decision dated August 15, 1960, in which after careful consideration of the qualifications of the petitioning creditors, he concluded that:

> "I find that on March 18, 1960, the four petitioning creditors had provable claims against the alleged bankrupt for the amount set forth above, which claims were and are liquidated as to amount, and are not contingent as to liability, which aggregated in excess of the value of securities held by Wurlitzer and WAC in a sum far in excess of the statutory

amount of $500; and that at the time of the bankruptcy the alleged bankrupt was insolvent, had committed the acts of bankruptcy as alleged in the amended petition, and had debts owing to creditors far in excess of the statutory amount of $1000.

Upon the pleadings herein, the record of the trial and the foregoing findings of fact, I am of the opinion that the petitioning creditors are entitled to an order and decree adjudging the alleged bankrupt as a bankrupt. (Section 18 Bankruptcy Act, Title 11 U.S.C. 41)."

Gibraltor claims error in the Referee's determination in that (a) the petitioning creditor, The Wurlitzer Company ("Wurlitzer") and the intervening creditors failed to sustain the burden of proof cast upon them by law, and (b) Wurlitzer and the intervening creditors were not qualified to act as petitioning creditors under the Bankruptcy Act.

Upon such a review this Court is subjected to the restraint of General Order 47 (11 U.S.C., following § 53) which provides that "The Judge shall accept his [the Referee's] findings of fact unless clearly erroneous." *Margolis* v. *Nazareth Fair Grounds & Farmers Mkt. Inc.*, 2 Cir. 1957, 249 F.2d 221, 223. The involuntary petition against Gibraltor was filed on March 18, 1960, to which Gibraltor filed its answer on March 29, 1960; leave was granted to Wurlitzer to file an amended petition on May 6, 1960, and on May 5 and May 6, 1960 the intervening creditors were permitted to intervene upon separate petitions, and thereafter on May 13, 1960 Gibraltor filed its answer to the amended petition. In his decision the Referee set forth the history of the case and outlined Gibraltor's contentions and the facts upon which his decision rested, all of which is unnecessary for this Court to repeat. The real issues before the Referee were the qualification of Wurlitzer as a petitioning creditor

and the qualifications of Wurlitzer Acceptance Corporation ("WAC"), William F. Wadsworth and Joseph Rae as intervening petitioning creditors. The petitions will be considered seriatim. In reaching his conclusion the Referee correctly decided certain peripheral issues which it is unnecessary to discuss upon this review.

WURLITZER

Gibraltor claims that Wurlitzer filed a sham petition in that it was prepared on the basis that Gibraltor had less than twelve creditors when, as a matter of fact, Wurlitzer knew otherwise and so prepared the petition with a view of later supporting the same by intervention of other creditors. It further claims that Wurlitzer received a fraudulent and voidable preference which it failed to surrender and for these reasons it was disqualified.

The Referee did not specifically rule on the claim of sham because it was not raised before him. However, all the evidence was before him and implicit in his finding that Wurlitzer had a provable claim is the fact that the petition was not based upon sham. While it was subsequently established that Gibraltor had twelve or more creditors at the time the petition was filed, there is nothing in the record indicating that Wurlitzer knew that Gibraltor had that number of creditors at that time. In fact, on September 11, 1959, a vice-president of Gibraltor (Alexander Goldberg) certified that as of that date Gibraltor had no creditors except Wurlitzer. Although Gibraltor raises the question whether Wurlitzer had a right to rely on this statement either at that time or subsequently, such statement nevertheless cannot be used as a basis for charging Wurlitzer with fraud as alleged by Gibraltor. Wurlitzer was not guilty of planned sham in filing its petition and the Court finds that there is no substance in this claim.

Referring to the second portion of Gibraltor's claim, the Court is of the opinion that the Referee's finding is

based upon the evidence and the law. A substantial part of the indebtedness owed to Wurlitzer by Gibraltor consisted of promissory notes in default secured by conditional bills of sale and in some instances by chattel mortgages. It is unnecessary to examine the details of Gibraltor's claim that Wurlitzer received preferential payments or transfers. Section 1, subdivision (11) of the Bankruptcy Act sets forth the definition of a creditor, and Section 59(b) of the Act sets forth the qualifications of petitioning creditors who have provable claims. Under the latter section three or more creditors with provable claims "liquidated as to amount and not contingent as to liability against any person which amount in the aggregate in excess of the value of securities held by them, if any, to $500 or over" may file a petition to have the debtor adjudicated a bankrupt. Assuming Wurlitzer were a secured creditor, this circuit has made it clear that Wurlitzer would not be disqualified by reason of this fact although its claim might not be allowed until the preference was surrendered. *In re Automatic Typewriter & Service Co.*, 2 Cir. 1921, 271 Fed. 1, 3; *Winkleman* v. *Ogami*, 9 Cir. 1941, 123 F.2d 78. The Referee found that Wurlitzer was an unsecured creditor for a sum far in excess of $500 and with this conclusion the Court agrees. Wurlitzer was therefore not disqualified because it was a secured creditor or received a preferential payment. *In Re Wm. J. Braun Builders, Inc.*, 6 Cir. 1958, 262 F.2d 107.

Wurlitzer Acceptance Corporation ("WAC")

WAC, a Delaware corporation and wholly owned subsidiary of Wurlitzer, was formed for the purpose of financing the sales of Wurlitzer's products sold by the stores owned and operated by Wurlitzer as well as those sold by Wurlitzer's dealers, distributors and operators. According to its balance sheet as of March 31, 1960, it had assets, made profits, was obligated on notes payable to banks and ac-

counts payable to Wurlitzer and paid Federal income taxes.

WAC's claim against Gibraltor is based upon two notes originally sold by Wurlitzer's New York distributor to Wurlitzer and subsequently assigned by Wurlitzer to WAC without recourse. One of the notes was executed by Phillip G. Hardy, dated April 29, 1958, in the amount of $6,238, and the other note was executed by Hewlett Vending Co., dated October 13, 1958, in the amount of $10,440. Both notes covered the purchase of Wurlitzer's juke boxes or phonographs from its New York distributor, secured by conditional bills of sale, and both were endorsed by the New York distributor to Wurlitzer which, in turn, assigned them to WAC for cash. On the date the petition was filed both of these notes were in default.

On May 15, 1959 Gibraltor executed and delivered a written guaranty of payment to Wurlitzer of all obligations of its New York distributor, which included the obligations of the distributor as endorser upon the notes above mentioned. The guaranty extended to Wurlitzer and to "its successors and assigns."

WAC's claim as a creditor has been challenged on a number of grounds, some of which need little discussion. For instance, the objection to the claim upon the ground that the notes were purchased by WAC without recourse is fictitious because there can now be little doubt that such an endorsement transfers title to the note or obligation. *Craig* v. *Parkis*, 1869, 40 N.Y. 181, 185; *North American Factors Corp.* v. *Motty Eitingon, Inc.*, N.Y. Sup. Ct. 1951, 105 N.Y.S. 2d 250, *aff'd*, 1951, 279 App. Div. 719, 108 N.Y.S. 2d 338, *aff'd*, 1953, 304 N.Y. 901. Moreover, based upon the wording of the guaranty, the assignment by Wurlitzer to WAC of the distributor's notes and obligations carried with it the guaranty by Gibraltor to Wurlitzer of the payment of all such notes and obligations, thus placing WAC as assignee in the position to assert a claim against Gibraltor upon such guaranty. *General Phoenix Corp.* v. *Cabot*, 1949, 300 N.Y. 87. Similarly, liability on a guaranty is a non-

contingent liquidated debt provable in bankruptcy (*Maynard* v. *Elliott*, 1931, 283 U.S. 273; *In re Rechtman*, D.C.N.Y. 1935, 11 F. Supp. 347) and WAC is not disqualified as a petitioning creditor because it holds security for the notes (*Winkleman* v. *Ogami*, *supra*; *In re Automatic Typewriter & Service Co.*, *supra*) or because others liable on the defaulted notes may have been called upon to pay the obligations. (See, *In re Mann*, D.C. Md. 1952, 117 F. Supp. 511; *Bibb Mfg. Co.* v. *Pope*, D.C.N.Y. 1925, 22 F.2d 557, *aff'd*, *per curiam*, 1927, 22 F.2d 558; *Loeser* v. *Alexander*, 6 Cir. 1910, 176 Fed. 265.)

Gibraltor's objection to WAC's qualification as a petitioning creditor is in essence based upon the fact that WAC is a subsidiary of Wurlitzer, the theory being that WAC's claim is not a separate claim but is in substance a part of Wurlitzer's claim. Gibraltor emphasizes the fact that Wurlitzer acted as collecting agency for WAC and that there was no privity between WAC and Gibraltor. This is simply another way of saying that the two corporations acted as one. At the outset it should be observed that there is nothing in the Bankruptcy Act or the authorities which *per se* prohibits a parent corporation and a subsidiary corporation from filing two separate claims against the bankrupt if they are in fact separate entities. It has been held that a parent corporation may place a subsidiary in involuntary bankruptcy (*In re H. Hicks & Son, Inc.*, D.C.N.Y. 1935, 10 F. Supp. 684, *aff'd*, 1935, 82 F.2d 277) and also recover its full claim from a bankrupt subsidiary in reorganization proceedings (*Comstock* v. *Group of International Investors*, 1948, 335 U.S. 211). Therefore, to sustain Gibraltor's challenge in this respect would require the Court to pierce the corporate veil of WAC and treat Wurlitzer and WAC as one corporate entity. The courts are reluctant to do this without proof that the parent corporation employed the subsidiary for an illegal or wrongful purpose or simply used the subsidiary as a front or cloak to accomplish an

illegal end or to perpetrate an injustice or fraud (*Rapid Transit Subway Construction Co.* v. *City of New York*, 1932, 259 N.Y. 472; *Jenkins* v. *Moyse*, 1930, 254 N.Y. 319; *In re Belt-Modes, Inc.*, D.C.N.Y. 1950, 88 F. Supp. 141; *Buechner* v. *Farbenfabriken Bayer Aktiengesell*, S.Ct. Del. 1959, 154 A. 2d 684) or to evade or avoid its public duty or obligation. *United States* v. *Morris & Essex R. Co.*, 2 Cir. 1943, 135 F.2d 711, 713. There is no such proof in this case. The formation of WAC was for an obvious legal purpose frequently resorted to by other corporations for business reasons and its separate entity was supported by its separate operations, assets and obligations. Here the association was free from guilt and the record is devoid of any evidence which would justify the Court in disregarding WAC's separate entity. It was therefore a qualified petitioner.

WILLIAM F. WADSWORTH.

Wadsworth was an employee of the bankrupt whose claim is for unpaid wages due him in the sum of $125. Gibraltor contends that $400 paid to Wadsworth while he was incapacitated for a period of ten weeks due to an accident, was a loan and converted Wadsworth from a creditor to a debtor to the extent of $275. The Referee found, and the evidence supports the finding, that the payment was in lieu of Workmen's Compensation and that Wadsworth has a provable claim for unpaid wages and was qualified to act as a petitioning creditor.

JOSEPH RAE.

Rae's claim is based upon the purchase by him and his partner Weintraub of certain locations and Wurlitzer's phonographs from Sandy Moore Distributors Corp. and Sandy Moore individually in September, 1959. He claims that the latter two were acting as agents for Gibralter, an undisclosed principal, and that he delivered to the agents

notes in the amount of $8400. The bill of sale listed the names and addresses of four locations and the serial numbers of juke boxes which had already been listed by serial numbers as the property of Gibraltor in a chattel mortgage previously delivered to Wurlitzer by Gibraltor. The notes were negotiated to Moore's brother-in-law Kerner, or to his corporation, SAK Trading Corporation. In November, 1959 Rae was sued on the notes although delivery of the locations and equipment was never made by the sellers to Rae. A settlement was then concluded whereby Rae and Moore apparently cancelled the purchase arrangement and Rae received back his notes but Moore refused to deliver them until after he endorsed his partner's notes. According to Rae's testimony, "from that point Sandy Moore took care of the payments of these notes because I and my partner did not make any further payments, or any payments, to be exact . . ." (R. 394). This presents a rather unique situation because there seems to be no reason for the endorsement by Rae.

In order to qualify as a petitioning creditor Rae's claim must not only be provable but it must be "liquidated as to amount and not contingent as to liability." Sec. 59 Bankruptcy Act, 11 U.S.C.A. § 95. If Sandy Moore and/or Sandy Moore Distributors Corp. were acting as agents for Gibraltor as an undisclosed principal, then Rae would have a provable claim in the sense that it is a reasonably fair and honest claim which a court of bankruptcy will hear. Such a claim may or may not be allowable dependent upon the proof adduced to establish it. *W. A. Gage & Co.* v. *Bell*, D.C. Tenn. 1903, 124 Fed. 371, 376; *Shapiro* v. *Lubasch*, S.Ct. 1945, 186 Misc. 182, 58 N.Y. S.2d 695. There is no question that the claim is "liquidated as to amount." (*In re Silver*, D.C. Ill. 1953, 109 F. Supp. 200, 203-204, *aff'd*, 7 Cir. 1953, 204 F. 2d 259), the only question being whether the claim is "contingent as to liability," which depends on

whether an act or event must occur before liability accrues. *In re State Realty Co. of Boston*, D.C. Mass. 1955, 131 F. Supp. 554, 556, *aff'd, sub nom, MacNeil* v. *State Realty Co. of Boston*, 1 Cir. 1956, 229 F.2d 358. Under the present state of the record, Rae is liable as endorser on his partner's notes, both Moore and Gibraltor as the undisclosed principal probably remaining liable to Rae under what vaguely appears to be an indemnity arrangement. At all events Rae's liability as endorser was contingent on his partner's default and if there were an indemnity arrangement, on default of Moore and Gibraltor. The record is silent as to whether or not there was any default on the notes either by Rae's partner or the indemnitors or whether or not the holder of the note had complied with the usual conditions precedent with respect to presentment, demand and notice, or that such requirement had been expressly waived. *In re Mann, supra.* Without a showing that these contingencies had been satisfied, Rae would not qualify as a petitioning creditor. In this posture the case would ordinarily be remanded to the Referee for further testimony but inasmuch as the other three creditors have fully qualified as petitioning creditors, such action will be unnecessary. On the present state of the record, the Court cannot find that Rae was a qualified petitioner. Gibraltor also points out that after Rae filed his petition a settlement was effected pursuant to which he received back his endorsed note. This would not affect Rae's status, however, since once the petition was filed the Court obtained jurisdiction and subsequent payment of the claim is immaterial. *Reed* v. *Thornton*, 9 Cir. 1930, 43 F.2d 813.

Settle order on two (2) days' notice within ten (10) days.

JOHN R. BARTELS,
U. S. D. J.

Office-Supreme Court, U.S.
FILED
OCT 28 1961
JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 429

GIBRALTOR AMUSEMENTS, LTD.,

Petitioner,

—v.—

THE WURLITZER COMPANY and WURLITZER ACCEPTANCE CORPORATION,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

EDWARD R. NEAHER
25 Broadway
New York 4, N. Y.
Counsel for Respondents

October 28, 1961

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Respondents, The Wurlitzer Company (hereinafter "Wurlitzer") and Wurlitzer Acceptance Corporation (hereinafter "WAC"), submit this brief in opposition to the petition of Gibraltor Amusements, Ltd., Bankrupt, for a writ of certiorari.

Question Presented

The only question presented upon this petition is this:

Whether the court below rightly rejected the contention that Congress, in writing the Bankruptcy Act, intended that a confessed hopelessly bankrupt corporation, no longer in business, may halt bankruptcy court administration of its remaining assets simply because one of its three peti-

tioning creditors is the wholly-owned subsidiary of another petitioning creditor, though parent and subsidiary are each a bona fide "creditor" of the bankrupt as defined in the Act, the subsidiary's separate claim arose long prior to bankruptcy as a result of the bankrupt's own act and admittedly was not purchased for the purpose of instituting bankruptcy proceedings, and no fraud or other wrong exists justifying disregard of the separate corporate entities.

The case is merely an application of the familiar rule that the separate corporate entities of parent and subsidiary will not be disregarded except to prevent fraud or other injustice, elements wholly absent here. On its peculiar, if not unique facts, the case involves no important or recurring question under the Bankruptcy Act requiring answer by this Court.

Statutes Involved

In addition to Section 59b of the Bankruptcy Act (11 U.S.C. § 95b) set forth at page 2 of the petition, the following provisions of the Act are pertinent:

> "§ 1. **Meaning of Words and Phrases.** The words and phrases used in this Act and in proceedings pursuant hereto shall, unless the same be inconsistent with the context, be construed as follows:
>
> • • • • •
>
> "(8) 'Corporation' shall include all bodies having any of the powers and privileges of private corporations not possessed by individuals or partnerships • • • ."
>
> • • • • •
>
> "(11) 'Creditor' shall include anyone who owns a debt, demand, or claim provable in bankruptcy, and

may include his duly authorized agent, attorney, or proxy."

* * * * *

"(23) 'Persons' shall include corporations, except where otherwise specified * * *."

Section 59e of the Act (11 U.S.C. § 95e) reads in part as follows:

"e. In computing the number of creditors of a bankrupt for the purpose of determining how many creditors must join in the petition, there shall not be counted * * * (2) * * * if the bankrupt is a corporation, creditors who are stockholders or members, officers or members of the board of directors or trustees or of other similar controlling bodies of such bankrupt corporation * * *."

Statement of the Case

Respondent Wurlitzer, an Ohio corporation, is a manufacturer of musical instruments, some of which are sold through retail music stores owned and operated by the Company and others through distributors or dealers. At its plant in North Tonawanda, New York, it manufactures coin-operated phonographs, popularly known as "juke boxes", which are sold nationally through franchised distributors. Respondent WAC, a Delaware corporation, was organized in 1957 as a wholly-owned subsidiary of Wurlitzer for the primary purpose of financing sales of Wurlitzer products generated by the retail music stores, distributors and dealers (R. 23a). There is no question that WAC was held out to lending banks as being operated as independently as any finance company, and that its separate entity was in fact supported by its separate opera-

tions, assets and obligations (R. 56a, 40a). The respective difficulties of Wurlitzer and WAC with petitioner arose out of the following peculiar circumstances:

Petitioner, a New York corporation, was engaged prior to bankruptcy in the business of operating a route[1] of some 400 to 500 Wurlitzer phonographs on Long Island, New York (R. 2a, 6a-8a; WR 54a).[2] Its owner and operating head was one Sanford J. Moore, who was also president and owner of Sandy Moore Manhattan Corp. of New York City (R. 7a). The latter corporation was formerly the New York area distributor for coin-operated phonographs manufactured by Wurlitzer and the sole supplier thereof to petitioner (WR 1a).

To acquire phonographs and auxiliary equipment for installation at its route locations, petitioner executed conditional sale contracts and promissory installment notes to Sandy Moore Manhattan Corp. (WR 2a). That corporation endorsed the notes and assigned the contracts to Wurlitzer, which accepted them in settlement of the distributor's account for phonographs sold and delivered (WR 2a, 7a). Each assignment was signed by Moore, as president of the distributor, and represented that the "accompanying

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[1] The operation of a juke box route consists of obtaining the right to place coin-operated phonographs and often games in a string of restaurants, luncheonettes, diners, taverns, etc., known as "locations" or "spots". The operator pays for the right by periodically splitting the coin box proceeds in some agreed proportion with the location proprietor. Aside from the initial cost of phonographs and games, the operator's expenses are normally confined to salaries for collectors and other employees, purchase of new records, and rent and other outlays incidental to the maintenance of a headquarters. This petitioner shared headquarters apparently rent-free in a building owned by one of Moore's many other corporations.

[2] The record references, unless otherwise indicated, are to pages of the respective printed appendices in the Court of Appeals, respondents' being indicated by "WR".

note or notes are genuine and enforceable" and that "the property has been delivered and accepted" (Exh. 16 *et seq.*). The same practice was followed with respect to the distributor's sales of Wurlitzer phonographs to other juke box route operators (WR 6a-7a). From its organization in October 1958 until mid-1959 petitioner acquired in this manner over 750 phonographs at an average wholesale cost of about $800 each, all ostensibly for operation on its route locations (WR 2a).

In addition to the indebtedness created by its own installment notes issued for this equipment, petitioner also became indebted to Wurlitzer and later to WAC under a written guaranty Moore had caused petitioner to execute and deliver to Wurlitzer on May 15, 1959 (WR 24a). The guaranty had been given in order to obtain for Moore's distributor corporation a continuance of shipments of phonographs on open account despite an already high credit extension on the part of Wurlitzer (WR 25a).

The guaranty in terms expressly extended to Wurlitzer and to "its successors and assigns" and applied to defaults in the payment of all notes covering phonographs purchased from the distributor. Two of such notes issued by third parties, which WAC acquired in the regular course of its business by purchase and assignment from Wurlitzer, are the notes involved in WAC's claim against petitioner under the guaranty (WR 12a, 18ab). One was a note of Hewlett Vending Co. acquired by WAC on October 31, 1958 and the other a note of Phillip G. Hardy acquired on May 28, 1959 (not 1958 as stated in the Petition, p. 4), both of which were in default by the date of bankruptcy (WR 12a, 48a-49a).

The events which led to the filing of the involuntary petition in bankruptcy date back to August 1959 when Wurlitzer, after a meeting with Moore, began to realize that

the distributor was in serious financial trouble (WR 32a; R. 48a). A proposal was made whereby Moore would be continued as a distributor provided petitioner continued scheduled payments on its notes (R. 48a). In the ensuing months Wurlitzer assigned a team of field investigators to visit each route location of petitioner in company with Moore's collectors. It was discovered that a substantial number of the phonographs supposedly sold to petitioner could not be located or accounted for. Further investigation revealed that others had been transferred to associates or relatives of Moore. At the same time, other purchasers from the distributor began to default on their notes claiming they had never received delivery of equipment and had signed contracts and notes only as an accommodation for Moore. Some of these acts are listed as the acts of bankruptcy (R. 4a-5a, 10a-11a).

A few days prior to the filing of the bankruptcy petition, Moore furnished Wurlitzer with a list of alleged creditors of petitioner which numbered only seven (WR 31a). Although the Referee found that petitioner had fifteen creditors other than Wurlitzer, WAC and one Joseph Rae (R. 27a-28a), following the adjudication and the expiration of the six-months period during which proofs of claim could be filed, only seven countable creditors including Wurlitzer and WAC (i.e., excluding five employee wage claimants) filed proofs of claim. Four were governmental agencies (tax and compensation insurance claims) which, though requested, declined as a matter of policy to intervene as creditors in support of the involuntary petition. The other was a friend of Moore who testified as a witness for petitioner in the trial on the petition (Steno. Tr. 537 *et seq.*).

Contemporaneously with the filing of the bankruptcy petition, a receiver was appointed by the District Court to operate petitioner's route in an effort to preserve the

remaining location rights and revenue for the benefit of creditors. Moore and several of his employees were employed by the receiver on a salary basis for this purpose. In late summer 1960 the receiver discovered that while acting in this capacity Moore and his associates had secretly removed and disposed of phonograph equipment owned by petitioner and had sold through nominees practically all of petitioner's remaining route locations to third parties. The matter was presented to the United States Attorney for the Eastern District of New York and resulted in Moore's indictment for criminal violations of the Bankruptcy Act, to which he later pleaded guilty.[3] These depredations reduced the revenue of the route to nil and forced the receiver to sell at public auction the remaining physical assets for a sum under $30,000.

Subsequently, the receiver became petitioner's trustee in bankruptcy and instituted a civil action in the United States District Court for the Eastern District of New York against Moore and the others who had participated in the conspiracy to defraud the estate.[4] On October 9, 1961, at the conclusion of a lengthy trial, the District Court in that action handed down a partial decision in favor of the trustee holding that the equipment and location rights involved therein were the property of the bankrupt's estate and had been illegally transferred as part of a plan and design to discharge Moore and his other corporations from indebtedness to some of the defendants but reserving decision as to the question of which alleged participants in the

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[3] This Court on October 9, 1961 denied Moore's petition for certiorari to review decisions of the lower courts refusing him permission to withdraw his guilty plea. *Moore et al.* v. *United States*, No. 196, October Term 1961.

[4] *M. Hallsted Christ, Trustee, etc.* v. *Vending Enterprises, Inc., et al.*, Civil Action No. 60-C-1207, U.S.D.C., E.D.N.Y.

conspiracy were to be held liable in damages. An attempt was made by some defendants before trial in that action to use these bankruptcy proceedings as a vehicle for a motion to stay its prosecution pending a petition for certiorari to this Court, but the court below (Judge Friendly included) unanimously refused to stay the trustee's administration of the estate.

The case, therefore, is one in which a confessed hopelessly bankrupt corporation, no longer in business, has been in the hands of the bankruptcy court for over a year and a half. During all that time the remaining assets have been in the process of orderly administration, and it would now appear after protracted litigation that som recovery for creditors is in prospect. The case is highly unusual on its facts; the question raised is of importance only to the litigants and unlikely to recur. If the administration of the bankrupt's estate were to be halted at this juncture on the ground that one of the petitioning creditors was not qualified, it would serve only to undo the orderly administration of assets and claims for which the Bankruptcy Act was enacted and leave each creditor to his own devices—a very unsatisfactory substitute in this case.

For the reasons hereinafter stated, respondents submit that the court below was clearly right in giving Section 59b literal effect in the circumstances of this case, and that the petition offers no substantial reason to support the conclusion that the case raises "an increasingly important problem in the administration of the Bankruptcy Act" (Petition, p. 9).

REASONS FOR DENYING THE WRIT

I.

Wurlitzer and WAC were each a bona fide "creditor" as defined in the Bankruptcy Act and entitled to be counted separately as such under the plain and unambiguous language of Section 59b.

The court below correctly held that the plain language of Section 59b and the purpose of the Bankruptcy Act permitted no other conclusion than that WAC was qualified as a petitioning creditor in the circumstances of this case. In reaching that conclusion, the Court paid strict heed to canons of statutory interpretation which have become familiar through many opinions of this Court.

The first of these is the rule that there is "no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes." *United States* v. *American Trucking Associations*, 310 U.S. 534, 543 (1940). As this Court pointed out in that case, when the words used are sufficient in and of themselves to determine the purpose of the legislation, "we have followed their plain meaning" (*ibid.* p. 543).

This rule the court below also followed, as it was required to do because of the express definition of "creditor" in Section 1(11) which Congress itself had supplied (Petition, App. 4a). It was the absence of such a legislative definition in the Motor Carrier Act which required this Court in *American Trucking Associations, supra,* to examine legislative history to determine the intended scope of the term "employees" used in that Act (310 U.S. at pp. 545-546).

No resort to Congressional debates of long ago is necessary or warranted in this case. The definition of "Creditor"

in Section 1(11) of the Act, viz., "*anyone who owns a debt, demand, or claim* provable in bankruptcy", is, as the court below underscored, a definition "virtually all-encompassing" with regard to the scope of permissible petitioners (Petition, App. 4a). Nowhere in the Act is there the slightest suggestion that "creditor", as so defined, is to be read any differently in Section 59b than in any other provision of the Act. Nor is any indication found in the Act even remotely suggesting that a parent-subsidiary relationship between two corporate petitioning creditors, each holding concededly bona fide separate claims against the bankrupt, deprives them of their normal right to be counted separately as creditors for purposes of the "rule of three." The plain language and purpose of the Bankruptcy Act is all to the contrary, as the court below demonstrated.

This Court has indicated that provisions in the Act relating to the satisfaction of the "rule of three" are to be given effect in accordance with their plain and unambiguous language. Thus, in *Canute Steamship Co.* v. *Pittsburgh & West Virginia Coal Co.*, 263 U.S. 244 (1923), cited in the petition (p. 6), although one of the original three petitioners failed to qualify due to lack of a provable claim, the petition was still held good because "the plain provisions of §59f supplementing and modifying the provisions of 59b * * * provide[s] in unambiguous language that creditors other than the original petitioners may, 'at any time' enter their appearance and 'join in the petition.'" 263 U.S. at 248.

The court below did not blindly follow the literal words of the Act. It properly considered the Act as a whole to ensure that a literal reading would not produce absurd or unreasonable results "plainly at variance with the policy of the legislation as a whole". *Ozawa* v. *United States*, 260 U.S. 178, 194, quoted in *United States* v. *American Trucking*

Associations, supra, 310 U.S. at p. 543. The court noted that the question of corporate relationships of one kind or another between creditors and a debtor had been expressly provided for by Congress in Section 59e of the Act.

Section 59e, incidentally, was amended to provide against improper use of corporate relationships when the Bankruptcy Act was completely overhauled in 1938 by the Chandler Act. Certainly, by that time Congress was fully aware of the problems posed by the multiple corporation means of doing business. This is borne out in the House Judiciary Committee Report submitted by Representative Chandler which recommended the amendments updating the 1898 Act. There it was stated:

> "In the modernization of the statute, every provision has been gone over with a view of bringing it into accord with the best feature of present-day business and commercial practice." (H.R. Rep. No. 1409, 75th Cong., 1st Sess., p. 4 [1937].)

The same report indicates that Congress was also fully aware that the Bankruptcy Act was no longer to be regarded as merely an equilibrium of tensions between debtor and creditor.[5] In this changed context, as the court below

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5 Quoted in the House Report, with apparent approval, were the conclusions from a 1936 report to a Special Committee of the United States Senate to Investigate Receiverships and Bankruptcy Proceedings and Administration of Justice in United States Courts, as follows:

> "Insolvency legislation in the past has been concerned solely with the regulation of the barriers designed to save unfortunate bankrupts from the rapacities of their creditors, and, conversely, to protect trusting creditors from the frauds of dishonest debtors. However, changing times have brought changing practices. The merchant who bought from a trade jobber has given way to the corporate retailer which owns its own factories. The trader who borrowed from his local bank has yielded to the debtor that sells its pledges in remote lending marts. Local partners have been supplanted by Nation-wide investors.
>
> "The consequence is that what was once a simple field of legislative conflict with two readily discernible and widely separated economic forces

pointed out, "the principal Congressional fear of abuse was not that a debtor would be too easily petitioned into bankruptcy—rather that through connivance with friendly creditors the insolvent debtor might be able unfairly to hamstring one or two large creditors" (Petition, App. p. 4a).

Clearly, when Congress was completely overhauling the Bankruptcy Act in 1938, and amending Section 59e to restrict the use of corporate relationships with creditors for the purpose of preventing involuntary bankruptcy, had it intended to place a similar restriction upon the right of related corporations to be counted as creditors in support of an involuntary petition, it would surely have done so. When such additional provisions could readily have been made but were not, it is not the function of the Court to read them into the Act. "It is [the Court's] judicial function to apply statutes on the basis of what Congress has written, not what Congress might have written." *United States* v. *Great Northern R. Co.*, 343 U.S. 562, 575 (1952). Cf. *United States* v. *Rice*, 327 U.S. 742, 752 (1946). In this case, the court below faithfully performed that function and there is no need for this Court to exercise its jurisdiction.

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has come to be a terrain populated by numerous, shifting, and kaleidoscopic contingents. Once the lines were finely drawn, now the boundaries are vague and indistinct; once the forces were wholly economic, now they are shot with social and ethical tinges. What once was legislative ground upon which information was little needed for a determination of problems and their remedies has become sanguinary with social and economic causes and effects." (*Ibid.*, p. 48.)

II.

The requirement of good faith pervading the Bankruptcy Act and the separate entity rule precludes this case from raising an important problem in the administration of the Act.

The record is clear in this case that WAC was an independently operated subsidiary, that Wurlitzer neither abused nor disregarded that independence, and that WAC's claims were acquired in the normal course of its legitimate business (Petition, pp. 6, 8).[6] On these admitted facts, the court below was clearly correct in treating Wurlitzer and WAC as separate legal persons under the familiar rule restated by this Court in *Scheuley Distillers Corp.* v. *United States*, 326 U.S. 432, 437, quoted at page 7 of the petition. As separate legal persons in fact according to law, Wurlitzer and WAC represent sufficiently separate creditor interests in reality, not merely in form, to satisfy the plainly spelled out requirements of Section 59b.

Such a holding raises no problem of importance to the administration of the Bankruptcy Act because it is neither inconsistent with the plain language of Section 59b nor subversive of the legislative purpose of the Act. As this Court has said, "the object of bankruptcy laws is the equitable distribution of the debtor's assets amongst his creditors; * * *." *Kuehner* v. *Irving Trust Company*, 299 U.S.

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[6] In this connection it should be noted that WAC did not acquire its creditor status "solely by purchase of debt claims from Wurlitzer" (Petition, p. 8). What WAC originally purchased was third party commercial paper which became claims against petitioner by reason of defaults not within WAC's control and as a consequence of petitioner's own act of guaranty which made such obligations enforceable against it by operation of law. Petitioner also disregards WAC's independent relationship to its own creditors, the banks which supply its working capital and look to it for payment (WR 46a-47a).

445, 451 (1937). That object can only be accomplished in this unusual case by preserving, not denying jurisdiction in the Bankruptcy Court.

The suggestion that counting parent and subsidiary as separate creditors in this case may do violence to the legislative purpose expressed in Section 59b (Petition, pp. 7-8) overlooks the basic safeguard of good faith built into the Bankruptcy Act. That good faith is the touchstone by which corporate relationships are to be tested under the Act is evident from this Court's opinions in *Comstock* v. *Group of Institutional Investors*, 335 U.S. 211 (1948) and *Taylor* v. *Standard Gas & Electric Co.*, 306 U.S. 307 (1939).

In *Comstock* a dominant parent corporation was allowed to recover its full claim from a bankrupt subsidiary in reorganization where its administration had been in good faith and the corporations were conducted as two separate entities, whereas in *Standard Gas* a parent corporation which had mismanaged its subsidiary for its own benefit had its claim subordinated to that of preferred stockholders.

The good faith rule as applied in this case and recognized by this Court provides the clear answer to the fears expressed in the petition that a significant problem of bankruptcy administration has been raised which deserves the attention of this Court. The fears expressed are founded upon imagined hypothetical situations not presented in this case. The very substitute suggested, namely, the identification of three "separate creditor interests" (Petition, p. 9), would not only read into the Act something which is not there but in the final analysis would require resort to the ultimate factual criterion of good faith.

As for the parcelling out of claims suggested in the dissenting opinion below (Petition, App. pp. 11a-12a), this Court has already taken care of the situation by Gen-

eral Order 5(2)—a rule clearly satisfied in this case and not intended to "prevent bona fide creditors from petitioning to have their debtor adjudged bankrupt" even when the separate creditors came into existence as the result of an assignment. *Reed* v. *Thornton*, 43 F.2d 813, 814 (9th Cir. 1930).

CONCLUSION

Petitioner's suggestion that the bitter Congressional debate between debtor and creditor factions preceding the Bankruptcy Act of 1898 may provide the true meaning of Section 59b is but an attempt to create doubt where there is none (Petition, p. 8). "The short answer is that there is no need to refer to the legislative history where the statutory language is clear. 'The plain words and meaning of a statute cannot be overcome by a legislative history which, through strained processes of deduction from events of wholly ambiguous significance, may furnish dubious bases for inference in every direction.'" *Ex Parte Collett*, 337 U.S. 55, 61 (1949), quoting *Gemsco* v. *Walling*, 324 U.S. 244, 260 (1945).

The issues involved in this peculiar case are of interest only to the immediate litigants. It presents no genuinely important problem of Federal law deserving the attention of this Court. Accordingly, the petition for a writ of certiorari to review the judgment of the Court of Appeals for the Second Circuit should be denied.

Respectfully submitted,

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October 28, 1961